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**BEFORE THE ARIZONA CORPORATION**

Arizona Corporation Commission
DOCKETED
JUL 25 2014
DOCKETED BY

COMMISSIONERS

BOB STUMP, Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

In the matter of:

TRI-CORE COMPANIES, LLC, an Arizona limited liability company,

TRI-CORE MEXICO LAND DEVELOPMENT, LLC, an Arizona limited liability company,

TRI-CORE BUSINESS DEVELOPMENT, LLC, an Arizona limited liability company,

ERC COMPACTORS, LLC, an Arizona limited liability company,

ERC INVESTMENTS, LLC, an Arizona limited liability company,

C&D CONSTRUCTION SERVICES, INC., a Nevada corporation;

PANGAEA INVESTMENT GROUP, LLC, an Arizona limited liability company, d/b/a Arizona Investment Center,

JASON TODD MOGLER, an Arizona resident,

BRIAN N. BUCKLEY and CHERYL BARRETT BUCKLEY, husband and wife,

CASIMER POLANCHEK, an Arizona resident,

NICOLE KORDOSKY, an Arizona resident,

Respondents.

DOCKET NO. S-20867A-12-0459

**SECURITIES DIVISIONS' POST HEARING REPLY BRIEF**

**Hearing Dates: October 21-23, 2013, February 18-20, 2014, May 6-8, 2014**

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The Securities Division ("Division") of the Arizona Corporation Commission ("Commission") submits this Reply in support of its Post-Hearing Brief ("Division Brief") and in response to the post-hearing brief submitted by Tri-Core Companies, LLC ("TCC"), Tri-Core Business Development, LLC ("TCBD"), and Jason Mogler ("Mogler") (collectively, "Tri-Core Respondents"). The Division will hereafter reference the Tri-Core Respondents' brief as the "Tri-Core Brief."[1]

The Tri-Core Brief is difficult to follow. Tri-Core Respondents appear to respond to the paragraphs of the Notice as opposed to addressing the evidence submitted by the Division at hearing. Further, Tri-Core Respondents fail to cite the administrative hearing record in support of their purported factual arguments, and in some instances, cite to what witnesses "failed to state." Any factual statements not supported by the hearing record should be stricken.

**A. Tri-Core Respondents Failed to Establish any Exemption.**

Tri-Core Respondents first ineffectively argue that the issuers of the various offerings are exempt from the registration requirements of A.R.S. § 44-1841. Tri-Core Respondents repeatedly argue a Rule 506 exemption, also known as the safe harbor non-public offering exemption, for the Tri-Core Mexico Land Development, LLC ("TCMLD") offering, TCC 2/08 offering, TCC 3/08 offering, TCC 6/10 offering, ERC Compactors, LLC ("ERCC") offering, ERC Investments, LLC ("ERCI") offering, and C&D Construction Services, Inc. ("C&D") offering. *See* Tri-Core Brief at pp. 2-4, 8-9, 12-14, 15-19, 38. Tri-Core Respondents also argue that the TCC 3/08 offering, TCC 6/10 offering, and ERCC offering, were exempt under A.R.S. § 44-1844(A)(1). *See* Tri-Core Brief, pp. 8, 10, 13-14. However, the issuers did not comply with Rule 506 or A.R.S. § 44-1844(A)(1), and no exemption applies for registration.

Under the Arizona Securities Act ("Securities Act"), the burden of establishing an exemption from registration is upon the party claiming it. *See* A.R.S. § 44-2033. Therefore, Tri-Core Respondents have the burden of proof of establishing the applicability of any exemption.

[1] Respondents ERC Compactors, LLC and ERC Investments, LLC did not submit any post-hearing briefing.

Our Supreme Court has held that, "[b]ecause of the vital public policy underlying the registration requirement, there must be strict compliance with all the requirements of the exemption statute." *State v. Baumann*, 125 Ariz. 404, 411, 610 P.2d 38, 45 (1980) (*en banc*). Tri-Core Respondents fail to meet their burden that an exemption exists for these offerings.[2]

15 U.S.C. § 77r provides for federal preemption of state registration requirements for "covered securities", which include a transaction exempt from registration pursuant to SEC rules or regulations, such as Rule 506. Regulation D of the Securities Act of 1933 outlines two exemptions and a "safe harbor" with respect to Section 4(2) of the Securities Act of 1933. Rule 506 provides a "safe harbor" to the private offering exemption under the Securities Act of 1933. A "safe harbor" is a rule that explicitly states the requirements an issuer *must* meet. If an issuer complies with *all* of the requirements of the rule, it will be deemed to have complied with the statute. In this case, if Rule 506 of Regulation D was complied with, the issuers would be deemed to have met the requirements for the section 4(2) private placement exemption.

However, there must be *actual compliance* with Rule 506[3] at the federal level before state registration requirements can be preempted. *See e.g. Brown v. Earthboard Sports USA*, 481 F.3d 901 (6th Cir. 2007). Actual compliance on the federal level is not a state-specific inquiry, and instead must include analysis of *all* offers and sales for that particular offering. A Rule 506 private offering exemption requires offers and sales satisfy the terms and conditions of 17 C.F.R. §§ 230.501 and 230.502 and contains substantive purchaser limitations. *See* 17 C.F.R. § 230.506.

An offering pursuant to Rule 506 must comply with Rules 501 through 503 of Regulation D. An issuer must establish that both: (1) the issuer does not use general solicitation to market the

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[2] Tri-Core Respondents also appear to argue that Mogler falls under an "issuer exemption", and therefore Mogler individually did not have to register as a dealer or salesman. Although Tri-Core Respondents fail to cite any legal authority (statute, regulation, case law) or facts from the record (for example, the statement that Mogler did not receive commissions appears nowhere in the administrative record) to support this argument, the Division has only asserted control person liability for Mogler, as outlined in the Division Brief. As a result, this argument will not be addressed outside this footnote.

[3] Because all of the offers and sales of the securities at issue occurred prior to the amendment to Rule 506, 17 C.F.R. § 230.506, in 2013, the language from the version in effect at the time of the offerings, and case law interpreting such language, is referenced.

securities (Rule 502(c)) and (2) the issuer sells its securities to no more than thirty-five (35) non-accredited investors who are sophisticated purchasers and an unlimited number of accredited investors (Rule 506(b)(2)). Further, when an issuer makes an offering pursuant to the registration exemptions provided by A.R.S. § 44-1844(A)(1) or A.A.C. R14-4-126, the issuer can conduct no "general solicitation" or "general advertising"[4] in connection with the sale of these securities[5].

1. General Solicitation Was Used In All Offerings.

Tri-Core Respondents cannot claim a Rule 506 or A.R.S. § 44-1844(A)(1) exemption because general solicitation or general advertising was used to market the securities for all of the offerings. Rule 502(c) provides that, "neither the issuer nor any person acting on its behalf shall offer or sell the securities by any form of general solicitation or general advertising . . .. " 17 C.F.R. 230.502(c). Rule 502 further states that general solicitation or advertising includes, but is not limited to, "any advertisement, article, notice or other communication published in any newspaper, magazine, or similar media or broadcast over television or radio" and "[a]ny seminar or meeting whose attendees have been invited by any general solicitation or general advertising." *Id.*

Here, the Division presented evidence that the TCC 3/08 offering, TCC 6/10 offering, and the C&D offering were advertised on a public radio broadcast called the Investment Roadshow.[6] Further, the referral source listed on the investor lists produced by Tri-Core Respondents for the TCMLD offering shows that several investors were solicited by radio/magazine[7], and one of the investors in the TCMLD offering confirmed he learned about the investment opportunity in a magazine.[8] Another investor testified that TCC solicited investors in the TCC 3/08 investment at a

[4] *See* 14-4-126(C)(3)

[5] The Securities Act does not include a definition of general solicitation or general advertising. A.R.S. § 44-1844(A)(1) and A.A.C. R14-4-126 contain provisions similar to federal law. In accordance with A.R.S. § 44-1815, we look to federal law for interpretative guidance. *See also e.g. Vairo v. Clayden*, 153 Ariz. 13, 734 P.2d 110 (App. 1987).

[6] Exs. S-21, S-23, S-26, S-38, S-44, S-47, S-221, S-224, S-227, S-229, S-230, S-255 (a), (b)&(c); HT Vol. II, p. 207, ln. 9 – p. 208, ln. 10, p. 209, ln. 25 – p. 212, ln. 4, p. 224, ln. 21 – p. 229, ln, 21, p. 231, ln. 25 – p. 232, ln. 23; HT Vol. IV, p. 408, ln. 22 – p. 413, ln. 15, p. 416, ln. 22 – p. 424, ln.22, p. 426, ln. 14 – p. 438, ln. 10, p. 438, ln. 11 – p. 444, ln. 9; HT Vol. V, p. 535, ln. 23 – p. 536, ln. 5.

[7] Ex. S-50.

[8] HT Vol. I, p. 85, lns. 8-20.

Los Angeles "vendor fair".[9] The investor list provided by Tri-Core Respondents also shows that several investors in the C&D offering were solicited by radio, and at least one investor confirmed the same.[10] While Tri-Core Respondents argue that the radio broadcasts did not offer any particular investment to listeners (*see e.g.* Tri-Core Brief, pp. 13, 21), this is contradicted by the radio broadcasts themselves, which were admitted at hearing *in their entirety*[11] in both audio form and by certified transcription. The radio broadcasts repeatedly reference investments available in Mexican land and recycling, make representations about the safety and security for the same, tell listeners how to use a self-directed IRA to invest in the companies, and invite listeners to call the Arizona Investment Center or go to the Arizona Investment Center website to schedule an appointment, or sign up for a seminar or webinar to learn about these "opportunities."[12]

Mr. Buckley, who acted as a salesman for all of the offerings at issue testified at hearing that offerees attended seminars, presentations, webinars in which he presented the investment opportunities both in Arizona and out of state.[13] In the Tri-Core Brief, Tri-Core Respondents argue that these seminars were "educational" and did not go into specifics about the offerings. This argument should be ignored because there is no evidence in the record that the seminars were simply educational. In fact, such a statement is contradictory to Mr. Buckley's testimony in which he confirmed the investments were discussed at seminars, presentations, and webinars (see above). Further, at hearing, testimony and documents were admitted confirming that investors learned about the investment opportunities through seminars/presentations/meetings.[14]

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[9] HT Vol. V., p. 633, lns. 11-21.

[10] Ex. S-35; HT Vol. II, p. 253, ln. 23 – p. 254, ln. 14.

[11] Tri-Core Respondents' statement that only portions of the radio broadcasts were read into the record at hearing is correct, but the full audio and certified transcriptions of the broadcasts are part of the record (*see* Exs. S-227, S-229 – S-231, S-255). Tri-Core Respondents were not precluded from reading any portion of the transcription or playing the audio from any of the broadcasts during hearing, but chose not to do so. Tri-Core Respondents also had the ability to cite to the full transcript(s) in their post-hearing brief, but also chose not to do so.

[12] Exs. S-227, S-229 – S-231, S-255.

[13] HT Vol. V, p. 533, ln. 8 – p. 535, ln. 23.

[14] Exs. S-115, S-139, S-176; HT Vol. I, p. 102, ln. 16 – p. 103, ln. 8, p. 167, ln. 20 – p. 168, ln.5; HT Vol. IV, p. 478, lns. 2 – 6, p. 493, lns. 1-15, p. 503, lns. 4-16, p. 504, ln. 22 – p. 505, ln. 13, p. 589, ln. 24, p. 590, ln. 3; p. 633, lns. 5-21, p. 652, ln. 21 – p. 653, ln. 4; HT Vol., p. 675, ln. 16 – p. 676, ln. 12, p. 688, lns. 7-23

The evidence also established that when offerees learned of the investment opportunities through radio, magazine, "vendor fairs", or attended meetings, seminars, presentations, and webinars, they had no substantive, preexisting relationship with the issuers. In determining whether a general solicitation has occurred under Rule 506 and A.R.S. § 44-1844(A)(1), the focus is on the relationship between the issuer and the potential investor. In making this determination, the SEC has focused on whether the issuer, or a dealer acting on behalf of the issuer, had a relationship with the offeree that was both "substantive" and "preexisting." *Woodtrails-Seattle, Ltd.*, SEC No-Action Letter, 1982 WL 29366 (Aug. 9, 1982); *E.F. Hutton Co.,* SEC No-Action Letter, 1985 WL 55680 (Dec. 3, 1985).

One way a respondent can establish the "substantive" element required under Rule 502 is by presenting evidence that only accredited investors (as defined in Rule 501(a)) were targeted for each offering. Tri-Core Respondents failed to do so in this case, and presented no argument in the Tri-Core Brief or facts at hearing to establish the same. In fact, the evidence at hearing established that unaccredited investors were solicited and sold the investments in *all* of the offerings at issue.[15] While investor questionnaires that allow the issuers to evaluate a prospective offeree's sophistication and financial circumstances may be used to establish the "substantive" element as well, the questionnaire must be *prospective*: the questionnaire cannot accompany the offering documents at issue. *See H.B. Shaine & Company, Inc.*, SEC No-Action Letter, 1987 WL 107907 (May 1, 1987). Although investor questionnaires accompanied many of the investment documents for each offering, there was no testimony or evidence that they were evaluated pre-offering and in fact, many of the questionnaires were dated on the same date the investment documents were executed, and many investors had no investor questionnaire, incomplete questionnaires, or questionnaires that were not filled out at all.[16]

[15] Exs. S-35, S-38, S-50, S-141 – S-143, S-145 – S-146, S-148 – S-150, S-154 – S-159, S-162, S-172, S-176, S-191 – S-193; S-208, S-210 – S-213, S-234; HT Vol. IV, p. 478, lns. 23-25, p. 505, lns. 18-20; HT Vol. V, p. 557, ln. 23 p. 558, ln. 8, p. 638, lns. 7-9, p. 656, lns. 2-16; HT Vol. VI, p. 680, lns. 14-16.

[16] *See e.g.* Exs. S-52, S-105, S-108, S-132, S-165, S-172, S-184, S-185, S-192, S-193, S-195, S-197, S-208, S-210, S-211, S-213.

Tri-Core Respondents not only failed to meet the "substantive" requirement, but they presented no evidence at hearing that investors and offerees had preexisting business relationships with *the issuers*. *See Woodtrails-Seattle, Ltd.*, SEC No-Action Letter, 1982 WL 29366. The business relationship had to have preexisted the time when the offering is being made. *See E.F. Hutton Co.*, SEC No-Action Letter, 1985 WL 55680. As the party asserting the exemption, it was the Tri-Core Respondents' burden to establish the preexisting relationship between the issuers and all investors and offerees. Again, Tri-Core Respondents failed to do so, and the evidence at hearing established just the opposite. Stevens admitted that he did not know the investors that invested with TCMLD, that they had no pre-existing relationship with TCMLD before investing, and could not identify how they were solicited.[17] TCC's representative admitted the same with regard to the TCC 3/08 offering – investors had no pre-existing relationship with TCC and he had no idea how they were solicited.[18] Multiple investors testified they had no pre-existing relationship with the issuers.[19] Even with the ERCI offering in which the Division proved one offer for sale had been made, Tri-Core Respondents presented no evidence regarding accreditation or sophistication of the offeree, or a pre-existing relationship between ERCI and the offeree.

Tri-Core Respondents appear to believe there is some type of "friends and family" exemption available, but no such language appears in Rule 506 or A.R.S. § 44-1844(A)(1). Tri-Core Respondents fail to provide any legal support for this argument.[20] Rule 506 and A.R.S. § 44-1844(A)(1), which say nothing about a family and friends exemption, clearly mandate requirements that Tri-Core Respondents failed to meet.

It is clear from the evidence at hearing, as well as the lack of evidence presented by Tri-Core Respondents, that general advertising and solicitation was used, and an exemption under Rule 506 and A.R.S. § 44-1844(A)(1) is unavailable for these offerings.

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[17] HT Vol. VII, p. 847, ln. 22 – p. 848, ln. 18.
[18] HT Vol. VIII, p. 1022, ln. 2 – p. 1023, ln. 23.
[19] HT Vol. IV, p. 478, lns. 19-22, p. 505, lns. 14-17; HT Vol. V. p. 558, lns. 3-5, p. 572, lns. 6-15, p. 651, lns. 16-22; HT Vol. VI, p. 677, lns. 16-23, p. 689, lns. 7-16.
[20] In fact, not only do Tri-Core Respondents fail to establish the legal basis for a "friends and family" exemption, but there was no evidence at hearing that *all* offerees and investors were friends and family.

2. Tri-Core Respondents Cannot Establish Unaccredited Investors were Sophisticated.

Not only do Tri-Core Respondents fail to meet the initial threshold of a Rule 506 and A.R.S. § 44-1844(A)(1) exemption because general advertising and solicitation was used, but they also cannot meet the second requirement of Rule 506: the securities for each offering must be sold to accredited investors and no more than thirty-five non-accredited investors who are sophisticated purchasers. *See* 17 C.F.R. § 230.506(b)(2)(ii). A sophisticated investor either alone or with a qualified purchaser representative "has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment." *Id.*; *see also Mark v. FSC Sec. Corp.*, 870 F.2d 331, 334 (6th Cir. 1989) (Respondent "is required to offer evidence of the issuer's reasonable belief as to the nature of *each* purchaser."). To obtain the *federal* exemption, and thus qualify to preempt any state registration requirement, *all* investors must be evaluated under this requirement, not just those in or from Arizona.

Each offering included unaccredited investors.[21] At hearing, Tri-Core Respondents failed to provide any evidence to establish that all unaccredited investors for each offering were sophisticated at the time of investment. Although it is not the Division's obligation to submit any evidence on this issue or *disprove* sophistication for unaccredited investors, there was evidence that unaccredited investors were not sophisticated. For instance, Stevens admitted that he did not know the investors that invested with TCMLD in the TCMLD offering,[22] and thus was not able to provide any substantive information about the unaccredited investors. TCMLD investor John Ploof testified he had never invested in Mexican land prior to the TCMLD investment, and there was no indication in the unexecuted investment questionnaires from Mr. Ploof or unaccredited TCMLD investor Jeanne Barnes that they were "sophisticated purchasers" for the Mexican land investment.[23]

[21] Exs. S-35, S-38, S-50, S-141 – S-143, S-145 – S-146, S-148 – S-150, S-154 – S-159, S-162, S-172, S-176, S-191 – S-193; S-208, S-210 – S-213, S-234; HT Vol. IV, p. 478, lns. 23-25, p. 505, lns. 18-20; HT Vol. V, p. 557, ln. 23 p. 558, ln. 8, p. 638, lns. 7-9, p. 656, lns. 2-16; HT Vol. VI, p. 680, lns. 14-16.
[22] HT Vol. VII, p. 847, ln. 22 – p. 848, ln. 18.
[23] Exs. S-50, S-105, S-108; HT Vol. IV, p. 478, lns. 19-22;

For the TCC 2/08 offering, the investor list shows that investors David Hickok, Martha Hansen, Kurt Senser, and Warren & Sue Schumacher were unaccredited investors,[24] yet their investment documents have unexecuted investor questionnaires and there was no testimony presented at hearing that these individuals were sophisticated purchasers.[25] The TCC 3/08 offering also included multiple unaccredited investors for which there was no evidence or testimony concerning their sophistication. Unaccredited investors identified themselves as having various occupations on their investor questionnaires such as an audio engineer, an account manager, a machine/motorcycle technician, and a teacher, but no further information was provided or requested of investors to allow a sophistication analysis.[26] Still other investors appear on the TCC 3/08 investor list that have no indication as to whether they were accredited or not,[27] and no evidence was presented by Tri-Core Respondents at hearing concerning these individuals' accreditation or sophistication.

For the TCC 6/10 offering, unaccredited investor Jessica Hogan testified that she had never invested in Mexican real estate before the investment with TCC, and there is nothing in the other unaccredited investors' questionnaires (at least one of which is blank) that indicates that they were sophisticated.[28] Further, the investor list supplied by TCC for the 6/10 TCC offering shows numerous additional investors in which there is no indication as to whether they were accredited, and no evidence was presented at hearing concerning their accreditation and sophistication.[29]

The ERCC offering investor list shows twenty-six unaccredited investors,[30] and no evidence was presented at hearing for several of those unaccredited investors to establish sophistication.[31] Again, for those unaccredited investors in which investment documents with

[24] Ex. S-50.
[25] Exs. S-128, S-132-S-135, S-220; HT Vol. IV, p. 491, ln. 13 – p. 501, ln. 8.
[26] Ex. S-141, S-142, S-148, S-150.
[27] Ex. S-44, *see e.g.*, investors Wixson, Mays, & Springer.
[28] Exs. S-184-S-188, S-222; HT Vol. VI, p. 680, lns. 11-16.
[29] Ex. S-47, *see e.g.*, investors Marsik, Neuenschwander, Marcus, Mays, Baldwin, Winkler, Sanchez, etc.
[30] Ex. S-38
[31] *See e.g.*, investors Jacobs, Holtzer, Smith, Rivera, Toshner, Garcia, etc.

investor questionnaires were admitted into evidence at hearing, there is no information that allows a sophistication analysis.[32]

The investor list for the C&D offering shows over ten investors that were unaccredited.[33] Not only was no evidence presented at hearing to establish sophistication for several of the listed unaccredited investors,[34] but no evidence was presented to establish that multiple investors listed as "accredited" were, in fact, accredited.[35] Even those unaccredited investors with investment documents that include investor questionnaires fail to establish sophistication.[36]

No evidence was presented either way for the ERCI offeree in terms of accreditation or sophistication, and it was Tri-Core Respondents' burden to do so.

Finally, Rule 230.502(b)(1) requires certain information be furnished to unaccredited investors: "When information must be furnished. If the issuer sells securities under § 230.505 or § 230.506 to any purchaser that is not an accredited investor, the issuer shall furnish the information specified in paragraph (b)(2) of this section to such purchaser a reasonable time prior to sale." Section (b)(2) requires substantive information about the offering be provided to unaccredited investors including, *inter alia*, "the same kind of information as required in Part I of a registration statement filed under the Securities Act" and a financial statement of the issuer. *See* 17 C.F.R. § 230.506(b)(2). Tri-Core Respondents submitted no evidence that the issuers for the offerings complied with this provision for any of their unaccredited investors, and thus fail to qualify for the Rule 506 exemption.

For these reasons, Tri-Core Respondents cannot meet the requirements to establish a Rule 506 exemption for any of the offerings.

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[32] Ex. S-191-S-193.
[33] Ex. S-35.
[34] Ex. S-35, *see e.g.*, investors Georgia Hsieh, Miltz, Adams, etc.
[35] Ex. S-35, *see e.g.*, investors Wieshaupt, Hass, Groves, Sanchez, Barba, etc.
[36] *See e.g.* Ex. S-210.

**B. Tri-Core Respondents Fail to Refute the Evidence of Fraud and Cannot Avoid Violations of the Antifraud Statute with an Exemption from Registration Provisions.**

Exemptions are inapplicable to the antifraud rules contained in both federal and Arizona securities laws. *See e.g.* 15 U.S.C. § 77q(c); *Little v. First California Co.*, 1977 WL 1054 (D. Ariz. 1977) ("Even though bank securities are exempt from the registration requirements of the 1933 Act, transactions in bank securities are not exempt from the anti-fraud provisions of either the 1933 Act or the 1934 Securities Exchange Act."); A.R.S. § 44-1991; *MacCollum v. Perkinson*, 185 Ariz. 179, 186, 913 P.2d 1097, 1104 (App. 1896) (holding that the statutory definition of a security for registration purposes is limited under A.R.S. § 44-1801(22) and the specified exemptions, but that the "securities fraud statute . . . includes the sale of even those securities that are exempted from the registration requirements."). Even if the securities at issue were exempt from registration – which they are not, as established above – they are not exempted from the antifraud provisions of A.R.S. § 44-1991.

Tri-Core Respondents attempt to refute some, but not all, of the fraud the Division established at hearing for the offerings. Due to the voluminous nature of the initial briefing on fraud for the offerings at issue, the Division will only address the assertions/arguments ineffectively made by Tri-Core Respondents in the Tri-Core Brief, but do not waive the additional fraud arguments raised by the Division at hearing and in the Division Brief.

Tri-Core Respondents' arguments are unsupported by the record and should be stricken and/or rejected.

1. Tri-Core Respondents Use the Incorrect Legal Standard for Fraud.

Tri-Core Respondents' first problem is that they argue the incorrect legal standard for an antifraud violation under the Securities Act. Arizona's standard for fraud is not the same as the federal standard under Rule 10b-5. Specifically, the federal rule requires intent or scienter, but there is no such requirement in Arizona. *See Eastern Vanguard Forex Ltd. v. Ariz. Corp. Com'n*, 206 Ariz. 399, 414, 79 P.3d 86, 101 (App. 2003); *Allstate Life Insurance Company v. Baird & Co.*,

*Inc.*, 756 F.Supp.2d 1113 (2010); *State v. Gunnison*, 127 Ariz. 110, 113, 618 P.2d 604, 609 (1980); *State v. Burrows*, 13 Ariz. App. 130, 474 P.2d 849 (1970). The Division does not have the burden of proving intent to violate, or knowledge that a respondent was violating, the Securities Act. A misrepresentation or omission of a material fact in the offer and sale of a security is actionable even though it may be unintended or the falsity or misleading character of the statement may be unknown. Stated differently, a seller of securities is strictly liable for any of the misrepresentations or omissions he makes. *See Rose v. Dobras*, 128 Ariz. 209, 214, 624 P.2d 892, 889 (App. 1981). Notwithstanding, there was no evidence at hearing that Tri-Core Respondents were unaware of any of the fraud at issue.

Further, regarding non-disclosure of the tax liens against TCMLD's principal, Stevens, for the TCMLD offering, Tri-Core Respondents appear to agree that this should have been disclosed to investors, but instead argue that only TCMLD's principal, Stevens, should have disclosed it to investors. *See* Tri-Core Brief, p. 24. This is not the law. It is a violation for *anyone* offering or selling securities to omit a material fact. *See* A.R.S. § 44-1991(A)(2). TCBD, acting as the dealer for the TCMLD offering (*see* Division Brief, pp. 34-35) omitted this material fact which constituted fraud.

2. Misrepresentation Regarding Salesmen Qualifications Regarding Commissions.

The investment documents for all of the offerings advised investors that the investment was "being sold by the officers and directors of the Company [TCMLD, TCC, ERCC, C&D], who will not receive any compensation for their efforts. No sales fees or commissions will be paid to such officers or directors. Notes may be sold by registered brokers or dealers who are members of the NASD and who enter into a Participating Dealer Agreement with the Company. Such brokers or dealers may receive commissions up to ten percent (10%) of the price of the Notes sold."[37] The Division presented evidence at hearing that conclusively established that individuals and entities

[37] *See e.g.* Exs. S-107 at ACC000165, S-128 at TRI_C007642, S-149 at TRI_C005972, S-187 at TRI_C003280, S-213 at ACC011099.

received sales fees or commissions that were not registered brokers or dealers with NASD (FINRA). *See* Division Brief, pp. 38-52.

Tri-Core Respondents unsuccessfully argue that an "issuer exemption", which purportedly exempts "officers, directors, and full-time employees" from registration. Unfortunately, Tri-Core Respondents cite no legal authority, and fail to establish how, even if such exemption exists and was applicable (*see* footnote 2, above), the fraud would be negated under an exemption. The investment documents affirmatively state that "*registered* brokers or dealers who are members of NASD" are allowed to receive commissions for selling the investments. Nowhere does it state that individuals that are exempt from registration may sell and receive commissions as well. This is important because a reasonable investor would likely rely on such a statement given that a registered broker or dealer has expertise in evaluating the investment before offering and selling it, especially when commissions are a motivating factor.

Further, even if there were some type of exemption for officers, directors, and full-time employees of the issuer, there is no evidence that Mr. Polanchek or his entities, who the Division established received significant sales fees for several offerings, were officers, directors, or full-time employees of the issuers. This argument should be rejected and these misrepresentations in the TCMLD, TCC 2/08, TCC 3/08, TCC 6/10, ERCC, and C&D offerings should be deemed violations of the antifraud provisions of the Securities Act.

3. Fraud Related to Ownership and/or Security for the Subject Offerings.

a. TCMLD Offering.

Tri-Core Respondents do not appear to dispute that TCMLD failed to purchase Lot 5 or to securitize investors as promised in the TCMLD offering. Instead, they assert that this issue has been addressed with investors by Stevens, that investors signed extensions, and TCMLD is working to resolve the issue. *See* Tri-Core Brief, p. 24. These statements (1) do not negate fraud, and (2) are contradicted by the evidence at hearing.

First, admitting to select TCMLD investors years after the investments were offered and sold that there are title issues with Lot 5 does not negate the fraud. The evidence at hearing established that the TCMLD investment documents represented that the notes being offered were "Secured Promissory Notes" and "are secured by the land Tri-Core Mexico Land Development, LLC purchases."[38] Nowhere did it state that TCMLD would not own the property. In fact, investors were told that TCMLD would own Lot 5 and securitize its investors with that land. First, despite representing that TCMLD was going to purchase the subject Mexican land, investors were not informed that an American entity cannot legally directly own the ocean-front Mexican property at issue; it must be held in a bank trust or a Mexican corporation.[39] Second, at least three investors were told that the investment was "safe" due to the security that was pledged.[40] Investors were not informed of any risk that that the land would not be purchased or their investments would not be secured.[41] It is axiomatic that one cannot pledge security in land it does not own. TCMLD has never purchased Lot 5, or any other Mexican real estate with investor funds, and has not securitized its investors in any way.[42]

Further, while there was evidence that *a few* TCMLD investors signed extension agreements *after* the notes came due, this does not negate the fraud that occurred during the offer and sale of the securities either. If anything, there is additional fraudulent conduct at the time the extensions were executed in that the title issues should have been disclosed to investors before

[38] *See e.g.* Ex. S-107 at ACC000154, 164; HT Vol. VI, p. 692, ln 1 - 7.

[39] Ex. R-14; HT Vol. VII, p. 833, ln. 19 – p. 835, ln. 7; HT Vol. VIII, p. 898, ln. 21 – p. 900, ln. 25, p. 990, lns. 3-25.

[40] Ex. S-104, S-109 at ACC010581; HT Vol. IV, p. 480, ln. 22 – p. 481, ln. 8; HT Vol. VI, p. 688, ln. 24 – p. 689, ln. 6, p. 689, ln. 19 – p. 690, ln. 19, p. 692, lns. 8-19.

[41] Tri-Core Respondents make a generalized argument that the PPMs for the offerings "contained plenty of language regarding different risks". *See* Tri-Core Brief, p. 38. Noting that most securities offerings contain cautionary language, federal courts have held that the materiality of the fraud is not negated by boilerplate warnings of risk. "Vague disclosures of general risks will not protect defendants from liability. Instead, the relevant cautionary language must be 'prominent and specific,' and must directly address 'exactly the risk that plaintiffs claim was not disclosed.'" *See In re MF Global Holdings Limited Securities Litigation*, 892 F. Supp. 2d 277, 204 (S.D.N.Y. 2013) (citation omitted). Tri-Core Respondents fail to cite to the particular language that purportedly adequately warned investors of any specific risk. For instance, the TCMLD PPM discloses some generalized boilerplate risks (as do all of the PPMs), *see* Ex. S-107 at ACC000168-169, but fail to address any specific risks. The TCMLD PPM states that investors notes are or will be secured by the land TCMLD purchases, but nowhere does it state that there is a risk that the land securing the investment will not be purchased at all or that there may be no security available.

[42] HT Vol. IV, p. 466, lns. 18-22; HT Vol. VI, p. 696, ln. 20 – p. 697, ln. 4; HT Vol. VII, p. 833, lns. 15-18; p. 835, ln. 13 – p. 837, ln. 13.

they signed the extensions. The testimony at hearing from three TCMLD investors that signed extensions establishes that, at the time they signed the extensions in 2011, they were not told about the title issue with Lot 5 that had existed since 2007, that TCMLD instead blamed the economy for non-payment on the notes, and told investors they could not afford the high interest rate.[43] It should also be noted that the argument that TCMLD intends to purchase Lot 5 does not correct the fraud either. This is simply a diversionary tactic to make it appear that TCMLD has the ability to repay investors when it does not. According to Stevens, even if title issues are resolved in favor of TCMLD, TCMLD has no additional funds to pay the remaining balance of the $1.7 million purchase price for Lot 5.[44]

b. TCC 2/08 Offering.

Tri-Core Respondents effectively have no response to the allegations of fraud concerning the TCC 2/08 Lot 5 investment. Instead, Tri-Core Respondents state that this PPM "was issued in error" and claim there is only one single note-holder for this offering. However, there is no evidence that this PPM was issued in error. According to documents produced by TCC, at least seven investors invested in the TCC 3/08 offering, with $335,000 raised from investors in or from Arizona.[45] It is difficult to believe that this offering was a mistake when TCC accepted funds from seven investors and Mogler signed the investment documents for seven investors. The Division established at hearing that there were numerous instances of fraud related to the offer and sale of the 2/08 investment (*see* Division Brief, pp. 41-43), none of which are negated by saying that the PPM was issued in error.

c. TCC 3/08 Offering.

With no citation to the administrative hearing record, Tri-Core Respondents argue that there is no fraud related to the TCC 3/08 offering (Lot 47/Relaxante) because TCC holds the

[43] *See e.g.* Ex. S-106, S-110, S-122; HT Vol. IV, p. 471, lns. 7-17, p. 490, lns. 2-9; HT Vol. VI, p. 700, ln. 12 – p. 701, ln. 2.
[44] HT Vol. VII, p. 828, ln. 23 – p. 830, ln. 10, p. 843, lns. 13-21, p. 844, ln. 22 – p. 845, ln. 2.
[45] Exs. S-30, S-32 at ACC004716, S-50, Exs. S-128 – S-129, S-132 – S-138, S-140, S-220; HT Vol. I, p. 127, ln. 4 – p. 129, ln. 23, p. 135, ln. 24 – p. 144, ln. 7.

"deed" to Lot 47, and there is no mechanism for securing investors with property in Mexico. This is directly contradicted by the evidence at hearing.

First, and undisclosed to investors, Lot 47 could not be held by TCC in Mexico due to Mexican laws. TCC's representative admitted that the 3/08 investment documents advised investors that TCC would own Lot 47, which was something that could not legally happen in Mexico.[46] In fact, the only relevant document at hearing was a Sales Agreement for Lot 47 with the purchaser identified as "Phoenix Premium Developers, Sociedad De Responsabilidad Limitada De Capital Variable", not TCC.[47] TCC's representative at hearing that Lot 47 is held by Phoenix Premium Developers, an S. de R.L. (Mexican corporation), and admitted that the land could not be held in fee simple title by an American entity.[48] This was a material misrepresentation. As a result, investors have not been provided proof that TCC purchased Lot 47[49] (which it did not since the Mexican entity, Phoenix Premium Developers, purchased it), or proof that they hold any security in Lot 47.[50] Second, TCC's representative admitted that there is a mechanism in Mexico to secure the TCC 3/08 investors with Lot 47, and also admitted that TCC 3/08 investors are not securitized by Lot 47 because it was too costly to TCC to do so.[51] Tri-Core Respondents' statement that investors did not want to be on title and that steps are being taken to securitize them (another diversionary tactic with no proof whatsoever) is not supported by any citation to the record and should be stricken.

Investors were never told that there was a risk they would not be provided any security, and in fact, the title of "Secured Promissory Notes" indicates the opposite. Given that the TCC 3/08 investment documents promised security in Lot 47, this was a material misrepresentation.

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[46] HT Vol. VIII, p. 1004, ln. 20 – p. 1005, ln. 3.
[47] Exs. S-45(a), S-45(b); HT Vol. I, p. 159, ln. 19 – p. 165, ln. 2.
[48] Ex. R-14; HT Vol. VIII, p. 900, ln. 4 – p. 907, ln. 19, p. 928, lns. 10-21, p. 990, lns. 9-11.
[49] Ex. S-45(a); HT Vol. V, p. 561, lns. 6-9, p. 574, ln. 13 – p. 575, ln. 18, p. 639, lns. 11-14.
[50] HT Vol. I, p. 186, ln. 13 – p. 187, ln. 7; HT Vol. V, p. 561, lns. 10-14, p. 575, lns. 19-23, p. 639, lns. 15-18.
[51] HT Vol. VIII, p. 1008, ln. 16 – p. 1011, ln. 15, p. 1035, lns. 6-8.

d. TCC 6/10 Offering.

Tri-Core Respondents argue that because a parcel in Mexico is "in process of being titled", there is no fraud related to the ownership and security for the TCC 6/10 offering. The TCC 6/10 investment documents advised investors that it was offering "Secured Promissory Notes" and that "[t]he Notes being offered by the Company in this Private Placement Offering are secured by the land Tri-Core Companies LLC purchases".[52] Investors were also orally advised their investment would be securitized by Mexican land.[53] Mogler further represented in a public broadcast during the time the TCC 6/10 investment was offered that investments in Mexican land were "safe" because they are secured by land.[54] At no point were investors advised of any risk that their investment would not be secured.

While TCC's representative testified that Lot 3, purportedly the subject of the TCC 6/10 investment, "is in the process of being titled,"[55] he also admitted that as of the date of hearing, Sylvia Torres owns Lot 3, not TCC, and could not explain why title had not been transferred from Ms. Torres.[56] Tellingly, until the hearing, there was no mention of Lot 3 to investors, some of which have had an investment outstanding for four years.[57] In fact, the evidence at hearing established that investors have never been provided any proof that their investment funds were used to purchase land in Mexico, and TCC failed to produce any title documents at hearing.[58] TCC's credibility as to the existence and purchase of Lot 3 is tenuous at best.

Even assuming the purchase of this Lot 3 is completed, TCC's representative admitted at hearing that due to Mexican law, title to a Mexican parcel such as Lot 3 cannot be held in fee simple by TCC and has to be owned by an S. de R.L. (Mexican corporation) or a Mexican

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[52] *See e.g.* Ex. S-187 at TCC_003269, 3279.
[53] *See e.g.* HT Vol. VI, p. 676, ln. 23 – p. 677, ln. 1.
[54] Exs. S-21, S-23, S-26, S-227, S-255(b); HT Vol. II, p. 207, ln. 9 – p. 208, ln. 10, p. 209, ln. 25 – p. 212, ln. 4, p. 224, ln. 21 – p. 229, ln, 21; HT Vol. IV, p. 408, ln. 22 – p. 413, ln. 15, p. 426, ln. 14 – p. 438, ln. 10, HT Vol. V. p. 535, ln. 23 – p. 536, ln. 5.
[55] HT Vol. VIII, p. 944, lns. 19-23.
[56] HT Vol. VIII, p. 1031, lns. 5-8, 12-17.
[57] Ex. S-222.
[58] HT Vol. V, p. 590, lns. 19-21; HT Vol. VI, p. 681, lns. 11-14; HT Vol. VIII, p. 1035, lns. 11-16.

national.[59] Thus, it was a material misstatement to represent to investors that TCC would own the land.

Finally, Tri-Core Respondents make the conclusory argument that investors will be collaterized with the property, but there is no evidence in the record as to how this will be achieved and why it was not done by now. Even assuming TCC takes title to Lot 3 (if Lot 3 even exists), there was no evidence at hearing as to how investors would be securitized in property the issuer, TCC, cannot own as a matter of law. TCC cannot securitize investors with property it does not own. Investors, some waiting four years, have been provided no proof that their investment is securitized with any Mexican land as promised in the investment documents.[60] Even assuming the purchase of Lot 3 is completed, TCC's representative has admitted that securitizing investors with property in Mexico is costly, and that TCC has no cash to securitize investors.[61] Investors were not advised of this risk, and the promise of a securitized note was a material misstatement.

e. ERCC Offering.

Tri-Core Respondents attempt to argue that, due to legal advice regarding a pending lawsuit, they chose not to purchase any equipment with investor funds. *See* Tri-Core Brief, pp. 12, 36. Not only is this argument unsupported by any testimony or evidence from the record, and thus should be stricken, even if it is considered, it does not provide any defense to the fraud asserted by the Division. The ERCC investment documents stated ERCC was a new division of "ERC", was in the business of recycling, and that "use of the proceeds is to purchase compactor equipment to be installed at commercial locations (SEE 'USE OF PROCEEDS')."[62] The ERCC investment documents further stated that ERCC was offering "secured Promissory Notes" and that the notes "will be secured by the equipment/compactors purchased."[63]

[59] HT Vol. VIII, p. 900, lns. 4-25, p. 990, lns. 9-11.
[60] HT Vol. II, p. 245, lns. 6-15; HT Vol. V, p. 590, lns. 7-18; HT Vol. VI, p. 681, ln. 23 – p. 682, ln. 1.
[61] HT Vol. VIII, p. 1009, ln. 16 – p. 1011, ln. 15; HT Vol. IX, p. 1104, lns. 13-18.
[62] *See e.g.* Ex. S-191 at ERCC_000309.
[63] *See e.g.* S-191 at ERCC_000305, 314.

Respondents provided no proof at hearing as to what happened with investor funds, and provided no proof that any equipment had been purchased as the ERCC investment documents promised. The statements regarding use of investor funds and securitization were material misstatements. Investors have been provided no proof that equipment was purchased by ERCC, nor any mechanism to securitize their investments.[64] In fact, based on the Tri-Core Brief, investor funds were not used for any purpose, much less as promised in the offering documents. Thus, the promise of regarding use of funds and securitization of the notes with equipment/compactors purchased with investor funds were material misstatements.

**C. Statements of Fact Unsupported by the Record Should be Stricken.**

Tri-Core Respondents had ample time and opportunity at hearing to present their case. In fact, Tri-Core Respondents requested, and were granted, a continuance of nearly *four months* to present their case after the Division presented its case in chief. *See* Eleventh Procedural Order. Clearly unable to establish certain "facts" at hearing, Tri-Core Respondents inappropriately use their post-hearing brief to assert "facts" that were never admitted through documentary evidence or testimony at hearing. *See e.g.* Tri-Core Brief, pp. 37-40.

Statements about what witnesses "failed to say" when giving testimony, and attempting to add facts that were never properly admitted (and that Tri-Core Respondents never attempted to admit) at hearing, including purported statements made by witnesses after leaving the stand, is inappropriate and should be stricken. For instance, Tri-Core Respondents were not precluded from cross-examining investor Mark Sherman, and Mogler and Mr. Hinkeldey did, in fact, cross-examine him. However, the factual recitation in the Tri-Core Brief regarding the details of Mr. Sherman's relationship with Mr. Polanchek, Mr. Polanchek's relationship with Mr. Sherman's mother, Mr. Sherman's discussions with Mr. Buckley concerning investor questionnaires,[65] and a

[64] HT Vol. V, p. 601, lns. 2-24.

[65] Tri-Core Respondents assert that Mr. Sherman failed to testify that Mr. Sherman told Mr. Buckley that filling out the investor questionnaire was not necessary and was at Mr. Sherman's directive. *See* Tri-Core Brief, p. 38. In fact, Mr. Sherman did not give such testimony and instead testified that Mr. Buckley assumed Mr. Sherman was accredited. *See* HT Vol. V, p. 622, ln. 22 – p. 623, ln. 8. Mr. Buckley gave no such testimony either.

purported arrangement regarding ERC Chicago are not a part of the administrative record.[66] These unsupported "facts" must be stricken and ignored.

Further, the statement regarding Tri-Core Respondents' inability to re-call Mr. Polanchek during the administrative hearing is also unsupported by any factual basis. Undersigned counsel never advised *any* witness that they would be arrested if they appeared for the hearing. Judge Stern provided Tri-Core Respondents with ample ability to call any witnesses they wanted, and Tri-Core Respondents never raised any issues regarding Mr. Polanchek's ability to testify. Notably, Tri-Core Respondents fail to state what testimony Mr. Polanchek was precluded from giving. In all likelihood, Tri-Core Respondents failed to recall him because he had nothing relevant to say, and his credibility at hearing was questionable, to say the least.

**CONCLUSION**

Tri-Core Respondents have ineffectively attempted to argue private offering exemptions when it is clear that none of the offerings fall within such an exemption. They have failed to meet their burden and these arguments should be rejected. Further, Tri-Core Respondents have selectively addressed *some* of the antifraud violations asserted by the Division at hearing, but ignored most of the evidence of fraud established by the Division. Where they have argued against a finding of fraud, Tri-Core Respondents have failed to cite to any facts or law that support their arguments. The Division has conclusively established numerous instances of violations of the antifraud provisions of the Securities Act for all of the offerings at issue, refuted any arguments Tri-Core Respondents have attempted to make in opposition to such evidence, and must be held responsible for such violations. Finally, the unsupported factual statements made by Tri-Core Respondents in the Tri-Core Brief must be stricken and disregarded.

[66] For instance, Tri-Core Respondents assert that Mr. Sherman failed to testify that Mr. Sherman told Mr. Buckley that filling out the investor questionnaire was not necessary and was at Mr. Sherman's directive. *See* Tri-Core Brief, p. 38. In fact, Mr. Sherman testified that Mr. Buckley assumed Mr. Sherman was accredited. HT Vol. V, p. 622, ln. 22 – p. 623, ln. 8. Mr. Buckley gave no such testimony either. The full transcription of Mr. Sherman's testimony can be found at HT Vol. V, pp. 583 - 626.

The Division requests that a recommended order be issued finding that the evidence at hearing supports an order against Mogler, TCC, TCBD, ERCC, ERCI, and C&D, ordering them to cease and desist, and with findings of registration violations, antifraud violations and control person liability as requested by the Division in the Division Brief.

RESPECTFULLY SUBMITTED this 25th day of July, 2014.

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